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Remarks: Copy of outline Document to Jim Cochrane (cat)
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THE WHITE HOUSE
WASHINGTON

CABINET AFFAIRS STAFFING MEMORANDUM

DATE: 3/1/82 NUMBER: 050171CA DUE BY: ---

SUBJECT: Cabinet Council on Commerce and Trade -- March 3 Meeting

	ACTION	FYI
ALL CABINET MEMBERS	☐	☐
Vice President	☑	☐
State	☑	☐
Treasury	☑	☐
Defense	☐	☑
Attorney General	☑	☐
Interior	☐	☑
Agriculture	☑	☐
Commerce	☑	☐
Labor	☑	☐
HHS	☐	☑
HUD	☐	☑
Transportation	☑	☐
Energy	☑	☐
Education	☐	☑
Counsellor	☑	☐
~~OMB~~	☐	☑
CIA	☐	☑
UN	☐	☑
USTR	☑	☐
CEA	☑	☐
CEQ	☐	☐
OSTP	☐	☐
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	☐	☐

	ACTION	FYI
Baker	☑	☐
Deaver	☐	☐
Anderson	☑	☐
Clark	☑	☐
Darman *(For WH Staffing)*	☑	☐
Jenkins	☐	☑
Gray	☐	☑
Beal	☐	☑
Mike Wheeler	☐	☐
Annelise Anderson	☐	☐
	☐	☐
	☐	☐
	☐	☐
	☐	☐
CCNRE/Boggs	☐	☐
CCHR/Carleson	☐	☐
CCCT/Kass	☑	☐
CCFA/McClaughry	☐	☐
CCEA/Porter	☐	☐

REMARKS: The Cabinet Council on Commerce and Trade will meet on Wednesday, March 3, at 8:45 AM in the Roosevelt Room.

The Agenda and briefing papers are attached.

NOTE: The paper for agenda item #1 on Trade Reciprocity, prepared by USTR is quite lengthly but you may wish to skim it.

RETURN TO: Craig L. Fuller
Assistant to the President
for Cabinet Affairs
456-2823

THE WHITE HOUSE

WASHINGTON

CABINET COUNCIL ON COMMERCE AND TRADE

March 3, 1982

8:45 AM

Roosevelt Room

AGENDA

1. U.S.-Japan Trade Issues /CM169
2. Steel Anti-Dumping and CVD Cases /CM96

RECIPROCITY IN U.S. TRADE

ISSUE

Notwithstanding the progress in international trade liberalization which has resulted from thirty years of Multilateral Trade Negotiations, there is a growing sense in certain quarters of the United States that the U.S. is not receiving access to the markets of other countries equivalent to that given them by the United States. This perception has been underscored by the fact that the U.S., like other trading nations of the world, is faced with the economic problems of high unemployment, inflation, payments imbalances which have reduced the real standard of living, and the increasing need for foreign exchange to purchase energy supplies. Given these economic circumstances, many nations are tempted to adopt - if they have not already done so - restrictive trade policies to shield their domestic industries from import competition; domestic subsidies to maintain employment; and government credits and similar trade-distroting incentives to increase exports. The result, however, is a vicious syndrome that misallocates resources, promotes incompetence, perpetuates inefficiency, institutionalizes market distortions, and leads to a cycle of trade inequities, declining real earnings, reduced savings and capital formation, slow or no growth, and inflation. In more and more nations, the calls for protectionism are louder and more pressing than they've been in several decades. Though United States policy has been and will continue to be one which supports free trade, there is also an increasing recognition that public support for that policy will not continue unless there is equity in the application of that policy. Though the alternatives facing the world trading system are narrowly limited, and the choice is critically important, it is unlikely that the U.S. can continue to tolerate unfair trading practices which adversely affect either our domestic market or our opportunity to trade elsewhere, especially given the difficult international economic situation. It is within this framework that an increasing discussion of "reciprocity in U.S. trade" has developed within the Congress and Executive Branch, and out of which there are new suggestions on how to deal with the problem. For example, a bill (S 898) was recently passed in the Senate which includes the concept of reciprocal market access for trade in telecommunications equipment. In the investment area, in spite of longstanding U.S. policy favorable and open to foreign investment, policymakers in the Congress and the Administration are considering measures which would modify or significantly change this policy. In addition, legislation of a more general nature requiring reciprocity in all U.S. trade has been introduced recently in this Congressional session. However, while it is clear why there is an increasing discussion of reciprocity in the U.S. and why some course of action must be taken to deal with unfair foreign trade practices, it is not clear what is meant by reciprocity nor how such a concept can be implemented.

In closely looking at the issue of reciprocity in U.S. trade, it appears that the U.S. faces two distinctly different problems. The first relates to the broader issue of whether or not the current international trading system, based on the principles of reciprocity and most-favored-nation treatment, still works to U.S. commercial advantage. That is, in negotiating trade concessions with certain U.S. trading partners and receiving reciprocal concessions from those countries, other countries - by virtue of most-favored nation treatment - have benefitted without necessarily granting any concessions to the U.S. Though we also benefit from MFN treatment accorded U.S. products through trade agreements made between other countries, several groups have suggested that the U.S. has benefitted less than other countries from the MFN trade negotiating process. This is particularly an allegation made by those groups (such as the general aviation industry) that have been subjected to totally free trade by reason of an MFN agreement (e.g., the Trade in Aviation Agreement) while their competitors from non-signatory countries operate with the protection of closed markets. The second and, perhaps, more pressing problem involves the imbalance in market access between Japan and the United States and what the U.S. can do about it. The Executive Branch needs to explore these elements of the reciprocity issue and determine exactly what reciprocity means and how it should be applied.

BACKGROUND

Definitions of reciprocity

Reciprocity can be defined in several ways. Congress provides a definition in Sections 104 and 126 of the 1974 Trade Act as "substantially equivalent competitive opportunities" (SECO) on a sector by sector or product by product basis. That is, the U.S., in negotiating trade agreements, would seek to obtain competitive opportunities for U.S. exports of appropriate manufacturing and agricultural product sectors equivalent to the competitive opportunities afforded in U.S. markets to like or similar products (e.g., cars for cars). If the President were to determine, up to five years after enactment of the 1974 Trade Act, that concessions made by other countries did not provide competitive opportunities for the commerce of the United States, he could take either general or product-specific action with that country to restore equivalence of competitive opportunities.

On the other hand, reciprocity can also refer to access in the broader sense of both tariff and non-tariff barriers and could be defined as a trade regime that allows the United States to sell in another country's market those products where it has a comparative advantage (e.g., U.S. agricultural products) in exchange for allowing that country to sell in the U.S. market those products in which it has a comparative advantage (e.g., Japanese autos). Apparent access however may not be an adequate guide to reciprocity. Reciprocity can also be measured by results, i.e., the success U.S. businesses have in selling particular products in a market relative to their success in other third country markets. In fact, one could even develop a performance-oriented test of reciprocity based on an objective assessment of what products the U.S. ought to be able to sell a particular country given our import competitiveness and performance in third countries. With a sense of what would have been sold in the absence of barriers, one could even estimate "lost trade."

Global reciprocity is yet a third concept. It refers to the fundamental GATT principal that the aggregate benefits of being a party to the GATT are substantially equivalent to the concessions given to all of the other members.

Status of reciprocity

Whatever one's concept of reciprocity, there is a need - both perceived and real - for a greater degree of reciprocity in current U.S. trade relations. This is particularly evident in our industrial trade with Japan. Notwithstanding the considerable amount of trade liberalization which has taken place, the U.S. today often finds itself frustrated in obtaining equivalent access to the Japanese market, as well as in dealing with the subtle non-tariff barriers and other anticompetitive practices frequently employed by other industrialized as well as many less developed countries. With regard to Japan, there are both obvious and hidden barriers to trade. On the obvious side, there are over twenty different GATT-illegal quotas, primarily on agricultural products, as well as a number of complicated and discriminatory barriers in the areas of standards certification, investment and tax policies, and a distribution system which prices imported goods out of the market. Moreover, Japan, in many areas, provides treatment to foreign products at a considerable disadvantage to that given similar Japanese products. This is a direct violation of GATT Article III (National Treatment on Internal Taxation and Regulation) which requires that products imported from one GATT member to another shall be accorded treatment no less favorable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, distribution, use, etc. Application of this rule to Japan is difficult, since Japan maintains both numerous administrative (i.e., illegal) and cultural (possibly legal except where encouraged by Japanese government action) barriers. Finally, in areas where it is clear that Japan has violated its GATT obligations, the U.S. has generally chosen to try and resolve these problems through bilateral consultations and negotiations rather than through the dispute settlement mechanisms of the GATT. Recent Japanese plans to liberalize their trade regime by advancing MTN tariff cuts on over 1500 products and reducing or eliminating over 50 non-tariff barriers is a response to the concerns of the U.S. and other countries. It is clear that it does not address the basic issue of reciprocity in U.S.-Japanese trade.

With regard to Canada, U.S. exporters find that they increasingly face barriers in the trade and investment area. Moreover, while the United States has a trade surplus with the European Community, U.S. exporters are hampered there by restrictive EC agricultural policies (e.g. the CAP) and must compete against tariff preferences that put them at a considerable disadvantage.

In addition, the U.S. faces a special problem with the developing countries - especially the NICs (Newly Industrialized Countries). Since they have not participated in all the rounds of tariff negotiations over the past thirty years, they retain high tariffs within generally restrictive trade systems. Yet, by virtue of the most-favored nation principle, NICs can take advantage of the concessions previously granted by the U.S. and other parties to the various rounds of negotiations. Thus, in future negotiations it will be difficult to encourage them to lower their tariffs and liberalize their trade because reductions have already taken place in the developed countries, and are binding upon them. This suggests a need to examine any possible additional leverage the U.S. can utilize to encourage our NIC trading partners to liberalize their trade regimes.

Finally, as U.S. investment and services transactions have become increasingly important, the need for greater reciprocity in these two areas has also become more evident - particularly since neither is covered within a particular international framework or set of obligations.

Reciprocity in the Investment Area

International investment issues, particularly trade-related ones, are becoming more and more important in the international economic area. A large number of countries, for example, are restricting or limiting foreign inward investment in certain areas, or are subjecting such investment to certain conditions, such as trade-related performance requirements. These actions often adversely affect U.S. investment interests in other countries. In addition, because of their trade-distortive nature, these actions often have a negative impact on U.S. trade interests.

Traditionally, the United States itself has maintained a very liberal policy toward foreign inward investment and not employed trade-related performance requirements. Moreover, the U.S. response to foreign investment restrictions and trade-related performance requirements has generally been low-key, with occasional attempts at bilateral persuasion.

As problems with other countries' foreign investment policies increase, however, it is necessary to reexamine traditional U.S. policies in this area to see whether they are adequate to deal with these problems. Many argue that U.S. legislative tools to deal with investment issues are not adequate, noting that the major deficiency in past U.S. policies and approaches being applied to today's international investment problems has been the lack of credible retaliatory authority by the President in the investment area. In other words, the President has been and is currently powerless, in their view, to retaliate in the investment area against other countries' unreasonable, arbitrary, or discriminatory acts against U.S. investment interests. Others argue, however, that the United States should not introduce its own restrictive practices and that, <u>in the long run</u>, restrictive foreign investment practices will correct themselves. Though this has not yet been resolved, various restrictive measures are being considered which would, for example, introduce a foreign investment screening process in the United States, impose a moratorium on foreign takeovers of U.S. energy and mineral companies, raise margin requirements and, regarding investment in the services sector, require independent regulatory agencies to take into account foreign barriers to U.S. service industries in granting the right to establish operations in this country.

Many of those who propose some form of restrictive U.S. action in the foreign investment area are concerned about non-reciprocal foreign practices, e.g., performance requirements, investment barriers, nationalization, expropriation, localization and a general lack of national treatment for U.S. investors. The countries cited most frequently for their lack of reciprocal treatment are Canada, France, Japan, Australia and many developing countries. Others, however, note that many countries placing substantial obstacles on U.S. investment are carrying out a policy that is applicable to all investors, including their own. It is in this area that controversy rages whether the U.S. should maintain an open investment policy to countries which, although not discriminating, do not allow "reciprocal" access to U.S. investments.

Reciprocity in the Services Area

It is becoming increasingly clear that service industries play a major role in the economies of all trading nations. It is also becoming clear that U.S. service industries face many barriers in their efforts to participate in the international marketplace.

The U.S. inventory of services trade barriers points to a pattern of problems encountered by U.S. companies. For example, in aviation some countries require U.S. carriers to use inefficient national monopolies for ground handling while the national carriers are allowed to set up their own and more efficient service. This practice poses a real competitive handicap to U.S. carriers operating in some markets. In other cases U.S. insurance companies are prohibited or forced to suffer long delays in obtaining access to national markets because of cumbersome and/or expensive licensing.

The pattern which is emerging indicates U.S. service industries are encountering a variety of non-tariff barriers, the causes of which are sometimes intentional and sometimes unintentional. These barriers can inhibit U.S. companies from establishing operations in some markets and restrict their ability to do business once they are there. Problems such as these call for appropriate authority to take action in order to assure reciprocity for U.S. concerns.

Consideration of the application of reciprocity to services should take account of the fact that the GATT in its present form does not apply to services. Currently, countries are not bound by an existing set of balanced international concessions for services in the way they are for goods. This is an important factor to keep in mind when establishing rules and principles which address problems of market access, rights of establishment, and discriminatory practices affecting services trade.

Because the service markets are not encumbered by existing trade regimes, an opportunity exists to apply reciprocity to services unilaterally, bilaterally, or multilaterally. Such flexibility will allow us to establish policy that takes into account the realities of the international service market rather than being bound by past concessions that are outdated or inappropriate in terms of their real impact in this area.

The principle of "equivalent competitive advantage" is as necessary and fundamental a rule in applying reciprocity to services as it has been to goods. It recognizes, for example, that the denial of access to a domestic market in retaliation for a similar foreign prohibition can lead to compounding and destructive trade restrictions. If we are to apply this same principle to services, however, we will need to keep in mind the unique nature of some service industries. Banking, for example, is governed by a complex set of state and federal rules which would require a major adjustment if the concept of equivalent competitive advantage were to be applied literally. In such instances policy must be sufficiently flexible to preserve sovereign rules governing banking, while at the same time recognizing the need to offset the resulting trade restrictions with equivalent concessions.

In the final analysis, our major goal in applying the principle of reciprocity to services should be to achieve a degree of political and commercial equivalency sufficient to remedy the major problems confronting service industries in their efforts to trade internationally.

<u>The historic perspective of reciprocity</u>

Given the trade problems we face with particular countries as well as in particular areas such as investment and services, the idea of seeking greater reciprocity is a sound and logical one. However, a close examination of how such a policy might be implemented, its implications for the

U.S. in terms of our obligations under the GATT, and how such a policy has been implemented in the past are all critical in determining an appropriate and effective reciprocity strategy today.

Traditionally, the terms "reciprocity" and "unconditional most-favored nation treatment (MFN)" have been used synonomously, just as non-reciprocity and conditional MFN have been. While unconditional MFN involves guaranteed equal treatment to all countries without requiring directly reciprocal compensation, conditional MFN has usually entailed either the denial of a trade concession to one country while giving that same concession to all other countries or the extension of a concession to a particular country without granting the same to any other country unless they, too, grant a reciprocal concession. Historically, most countries' MFN policies - whether conditional or unconditional - have been applied to tariff negotiations and concessions, more so than non-tariff barriers.

With regard to tariffs, the U.S. as well as the international community as a whole has had a long history with both conditional and unconditional MFN. Though the unconditional form of MFN (i.e., guaranteed equal treatment without requiring directly reciprocal compensation) was used exclusively until the late 18th century, the United States was the first to use conditional MFN starting in 1778. This was then adopted by the Europeans and spread to Latin and Central America to become common in treaties during the first half of the 19th century. The wave of liberalism and free-trade sentiment that swept Europe in the second half of the 19th century brought a return to the use of the unconditional MFN clause with the negotiation in 1860 of the Anglo-French Cobden Treaty. However, while European countries ultimately returned to the the unconditional form, the United States during the late 1800s and early 1900s negotiated treaties and agreements which accorded preferential tariff treatment to the goods of certain countries which made reciprocal concessions without providing the same treatment to the goods of other U.S. trading partners. These treaties or agreements were intended to insure non-discriminatory treatment of American goods while addressing the high tariffs on manufactured goods which existed at that time. Though in practice only a limited amount of U.S. trade was affected by reciprocal treaties involving conditional MFN, it was not until 1923 that the U.S. abandoned this practice. By the close of World War I the U.S. was a leading world power and could no longer afford to be without a positive foreign economic policy. This was particularly true since it had found that the conditional most-favored-nation policy had become a source of friction and ill-will rather than an instrument with which to end discrimination against U.S. products. Because those countries who were not accorded tariff concessions granted to other U.S. trading partners typically felt that they had been discriminated against, they would demand that their products be given the same treatment and would threaten retaliation if not given equal treatment.

In 1919 the U.S. Tariff Commission (in existence then for three years) issued a comprehensive report on "Reciprocity and Commercial Treaties" and, though it made no recommendations, clearly concluded that it would be desirable to adopt an unconditional MFN policy. In this report the Commission said: "So far as commercial policy and commercial negotiations are concerned, the evidence presented in the present report indicates that a policy of special arrangements, such as the U.S. has followed in recent decades, leads to troublesome complications. Whether as regards our reciprocity treaties or as regards our interpretation of the most-favored-nation clause, the separate and individual treatment of each case tends to create misunderstanding and friction with countries which, though supposed to be not concerned, yet are in reality much concerned. When each country with which we negotiate is treated by itself, and separate arrangements are made with the expectation that they shall be applicable individually, claims are nonetheless made by other States with whom such arrangements have not been made. Concessions are asked; they are sometimes refused; counter concessions are proposed; reprisal and retaliation are suggested; unpleasant controversies and sometimes international friction result." Thus, the U.S. changed its trade policy to reflect its broader export interests at that time, and expected that by offering complete and continuous non-discriminatory treatment, the U.S. would obtain the same treatment from other countries and would, hence, reduce discrimination against U.S. exports. Authority for the U.S. to offer unconditional MFN was included in the Tariff Act of 1922 and implemented in 1923. The Trade Agreements Act of 1934 included an unconditional MFN provision and made it a requirement of U.S. domestic law.

MFN today

Though application of MFN treatment - whether conditional or unconditional - has largely been with regard to tariff concessions or negotiations, the principles of unconditional MFN and reciprocity have formed the underlying basis for all of the tariff as well as non-tariff negotiations which have taken place in the GATT since its formation, and provide the cornerstone of the international trade rules embodied in the GATT. The basic rationale for unconditional MFN is that if every country observes the principle, all countries will benefit in the long run through the resulting more efficient use of resources. Furthermore, if the principle is observed, there is less likelihood of trade disputes. In fact, the basic idea of MFN in the GATT context is that discrimination in any form is likely to lead to more discrimination, and that in the long run all countries will suffer from the inevitable distortion of trade patterns which will arise out of discrimination (as witnessed in the tariff wars of the 1930s). In order to prevent a country or pair of countries from implementing such policies and thereby setting off a chain reaction, the GATT has attempted to obtain the simultaneous pledge of the largest possible number of trading countries that they will not discriminate against each other.

Problems with Reciprocity and Unconditional MFN

However, aside from the country-specific problems we face, the unconditional MFN principle - as practiced to date - raises some critical questions and issues for the U.S. in today's international trading system. First, the initial tariff-cutting negotiations based on the unconditional MFN principle (which included the 48 original GATT members) never envisaged a trading system where some one hundred countries would later be involved and where so many would be able to take advantage of the substantive concessions made by so few.

Second, despite the considerable tariff cuts which have been made on thousands of products in international trade, countries have increasingly used non-tariff barriers and even invented new NTBs to compensate for the lower tariffs. Finally and, perhaps, most important, GATT has not guaranteed reciprocity and the unconditional MFN principle has not been scrupulously observed in the GATT by the Contracting Parties. In fact, the MFN principle may currently be observed more in the breach than in practice, and there have been deviations from the principles of reciprocity and MFN - some of which have been legal and others illegal under the GATT. For example, under GATT Article XXIV, customs unions and free trade areas can be established in which products of certain countries are given preferential treatment without doing so for other GATT members. The current extent of preferential trade under this article was not envisioned by the authors of the GATT. Further, the EC preferential agreements with the Lome countries and those of the Mediterranean litoral further corrupt the MFN principle. Another GATT-legal deviation from MFN is the extension of differential and more favorable treatment to developing-country members of GATT. Under the 1979 agreement on "Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries" (more popularly known as the "Enabling Clause"), GSP schemes, intra-LDC preferential arrangements, and special treatment for the least developed countries (LLDCs) are now legally and permanently provided for in the GATT. As to GATT-illegal deviations from the principles of reciprocity and unconditional MFN treatment, one might cite the numerous non-tariff barriers established by many GATT members to protect particular products and sectors from competition, as well as the numerous policies which give national products special treatment not accorded to similar imported products - the latter of which violate Article III of the GATT.

Limited reciprocity

Even the newly negotiated non-tariff barrier codes of the GATT contain deviations from MFN in that the rights and obligations of most of the codes apply only to the respective signatories. In fact, one might even define the new non-tariff barrier codes in standards, government procurement, licensing, subsidies, etc. as models for limited reciprocity since the U.S. currently applies the codes only to those countries which gave mutually advantageous opportunities to the U.S. While only a first step, the U.S. is already beginning to ensure that reductions in U.S. NTBs are offered only to those U.S. trading partners who have also reduced their NTBs and have taken on the responsibilities of the NTB codes.

Costs of reciprocity

On the other hand, the conditional application of MFN between code signatories and non-signatories does not in any way detract from the application of MFN amongst signatories to the respective codes. Even in areas not covered by the NTB codes, Article I of the GATT provides that any advantage, favor, privilege or immunity granted by any GATT member to any other country shall be accorded immediately and unconditionally to all other GATT members. Thus, any attempt by the U.S. to implement a policy of reciprocity which entails conditional MFN could possibly lead to disputes regarding our obligations in the GATT and under the non-tariff barrier codes. The U.S., for example, allows foreign car manufacturers - including the Japanese - to self-certify the safety standards of those cars. In contrast, however, the Japanese deny the U.S. and all other foreign car manufacturers the ability to certify their own auto standards. Should the U.S. decide to alter its treatment of Japanese autos with regard to standards self-certification but continue present certification practices with regard to, say, German and British autos, the Japanese could invoke the MFN provisions of the Standards Code and/or those of the GATT. That is, because the Japanese policy is non-discriminatory and applied to all countries on an MFN basis, while the U.S. policy would discriminate against Japan, such action would violate U.S. MFN obligations in the GATT and would likely lead to some form of retaliation by the Japanese. Alternately, in order not to violate the MFN provisions of the GATT and/or the Standards Code, the U.S. would have to apply the revised self-certification procedures to all autos imported into the U.S. market whether Japanese or not. While this may, in fact, result in "reciprocity" in this area between the U.S. and Japan, it might destroy the balance between the U.S. and Germany or Britain, and could lead to some form of retaliation from them.

The danger, then, of the U.S. attempting to pursue equity and reciprocity in its trade relations is, first, that we risk violating our obligations under GATT <u>if</u> such a policy is implemented through conditional MFN treatment - i.e. withdrawal of MFN on particular products from a specific country. While intentional violation of U.S. obligations under GATT is one of many options which might be considered in looking at ways to gain reciprocity in U.S. trade, it is one whose pros and cons should be carefully weighed. The second danger in seeking reciprocity through conditional MFN lies in the potential costs to U.S. sectors which are competitive in both production and export, such as computers and aircraft equipment. That is, a policy of reciprocity implemented by withdrawing MFN from specific countries on specific products - once started between trading partners - may not always take the form of "cars for cars," but could mean Nation A might respond to Nation B's withdrawal of access to its market in cars with the denial of access to its own market in beef, for example. Finally, some U.S. trading partners may themselves adopt the concept of reciprocity and apply their own version of it to U.S. sectors traditionally "protected" or, potentially more harmful or costly, might aim their "reciprocity" actions at the most productive and competitive U.S. sectors.

Conclusions

The need for reciprocity:

On the one hand, there is the recognition that despite the flaws in application, the reciprocal bargaining process which has occurred under GATT auspices for the last three decades is largely responsible for the substantial lowering of tariff barriers specifically and for any liberalization of non-tariff barriers which has thus far occurred. There is, on the other hand, a recognition that the long-standing policy of unconditional MFN does not adequately address the problems facing the international trading system today. As non-tariff barriers have increasingly appeared to replace the lowering of tariffs and as barriers in areas never covered by GATT such as services and investment have increasingly thwarted U.S. trade, the need for greater reciprocity in U.S. trade relations has become more evident.

The issue then is how to institute a U.S. policy aimed at increasing reciprocity with our trading partners without necessarily tearing down the present international trading system, reversing its benefits to date, or starting a spiral of protectionist actions.

<u>What should it mean:</u>

Reciprocity should, generally, mean that the U.S. should seek equal access to other countries' markets to sell those products we produce and export most efficiently, in return for allowing other countries to export to the U.S. market those products they produce most efficiently. Reciprocity should not mean equivalent access on a sector by sector or product by product basis, and, by all means, should not be a guise for protectionist actions. Most important, the need for reciprocity should not be determined by whether or not the U.S. has a trade deficit with a particular country. Recent arguments that use our trade deficit with Japan as evidence that we do not obtain "reciprocity" from them are dangerous. While the U.S. trade deficit with Japan makes their trade barriers even more intolerable, the existence of a trade deficit should not be the basis of U.S. policy towards Japan. If such an argument were to be used by the

U.S. against Japan, we risk that same argument being used by the Europeans, for example, with whom we have a trade surplus. Reciprocity should refer, instead, to the state of overall balance in our bilateral trade relations.

How should it be implemented:

The primary and preferable method for obtaining "reciprocity" should be by seeking liberalization of foreign markets rather than by raising equivalently restrictive barriers in our own.

Whether mandated by reciprocity legislation or not, barriers should be catalogued by country, noting whether they are covered by the GATT, what measures might be taken there, and how the country can be encouraged to remove those barriers before offsetting actions are taken. In areas such as investment which are not covered by GATT, the establishment of an international framework of obligations or guidelines should be the first step in ensuring greater reciprocity. In the continuing absence of such guidelines, however, thought should be given to how domestic legislation (such as Section 301 of the Trade Act of 1974) can be revised to provide for appropriate reciprocal actions. With regard to service industries, which are not covered by the GATT, we will also need to establish an international framework for achieving reciprocity. In the absence of such a framework, we have employed existing legilation (Section 301 and other appropriate regulatory legislation) and should investigate new legislation which deals more specifically with the problem of reciprocity in services. While authority to act must be discretionary, taking into account the potentially detrimental impact on the U.S., it must be applied decisively. In the last analysis, the principle U.S. weapon for assuring open markets for services industries is the capability for limiting or denying market access where foreign barriers are insurmountable. This might even include extending to regulatory authorities, such as the FCC, the provision to consider reciprocity in granting foreign licensing decision upon consultation with the Executive Branch as to its international trade implications.

Whether covered by GATT or not, negotiations should be initiated specifically addressing those barriers identified and taking whatever measures earlier determined as necessary to encourage their removal.

In the case of identified barriers which are illegal under GATT, negotiations under GATT's dispute settlement mechanisms should immediately be initiated <u>in addition to</u> bilateral efforts to add further leverage in getting them removed.

In the case of identified barriers which are not clearly illegal under GATT (such as the auto self-certification problem with Japan), bilateral negotiations should begin which make it clear that after a specified period of time (e.g. 8 months), the U.S. will take certain predetermined offsetting actions which will restore reciprocal relations in that area.

Where it becomes evident that efforts - both bilateral and multilateral - to encourage liberalization in other countries' markets are to no avail, the U.S. should then, and only then, raise equivalent and offsetting barriers. Since, however, our GATT obligations provide little flexibility in the tariff area, these offsetting barriers should be concentrated in - but not limited to - the non-tariff barrier area. To the extent possible, actions should be carefully crafted to affect primarily the country not providing reciprocity. However, such offsetting actions should be applied on a non-discriminatory basis and should allow the U.S. to adhere to its international obligations. That is, if at all possible, U.S. offsetting actions should not take the form of conditional MFN by denying or withdrawing from one country treatment which we continue to give to all others. If such discriminatory action is intentionally taken against a particular country on a specific product on the chance that they will not want to risk mutual recriminations in the GATT, this should be done with the understanding that the GATT and the world trading system as we know it could be undermined.

THE SECRETARY OF COMMERCE
Washington, D.C. 20230

MEMORANDUM FOR: Members of the Cabinet Council on Commerce and Trade

FROM: Malcolm Baldrige, Chairman pro tempore
Cabinet Council on Commerce and Trade

SUBJECT: Steel Update

ACTION FORCING EVENT:

On January 11, 1982, seven U.S. steel producers filed antidumping and countervailing duty complaints against steelmakers in eleven foreign countries. In response, the steel trigger price mechanism (TPM) was suspended.

STATEMENT OF ISSUE:

The Department of Commerce (DOC) is currently investigating whether steel producers in 15 foreign countries have sold unfairly subsidized or dumped steel in the United States. The largest volume of trade under investigation involves the European Communities. If DOC finds dumping or subsidization and the International Trade Commission (ITC) determines that the U.S. steel industry has been materially injured, or is threatened with material injury, duties will be imposed to offset the unfair trade.

The investigations are of great concern to several countries and to the European Communities because of the possibility that prohibitive duties may be imposed. The loss of the U.S. market to these countries would mean a further deterioration of already faltering steel industries, with attendant economic, social, and possibly political difficulties. In addition, as steel is diverted from the U.S. market to other export markets, the prospect of chaotic competition looms large to all major steel producers, including those not involved in the current investigations (particularly the Japanese).

ANALYSIS:

Recent Events: Complaints Filed and TPM Suspended

On January 11, 1982 seven U.S. steel producers filed antidumping and countervailing duty complaints against producers in eleven foreign countries (Belgium, Brazil, Federal Republic of Germany, France, Italy, Luxembourg, Netherlands, Romania, South Africa, Spain, and United Kingdom). Because the TPM was a substitute for, not a supplement to, individual complaints by steel producers, it was suspended upon receipt of the petitions. The personnel that had been administering the TPM are now processing the antidumping and countervailing duty investigations.

On February 1, 1982, DOC initiated investigations in 109 of the 132 cases filed by the industry. Sixteen petitions were withdrawn and seven were dismissed as legally insufficient. On February 18, the ITC terminated 54 of the 92 cases before it by finding no reasonable indication of material injury or threat of material injury (17 of the cases, involving South Africa and Spain, were not referred to the ITC because those two countries have not signed the international Subsidies Code and therefore do not get an injury test).

The investigations that remain active comprise 90 percent of the import tonnage covered by the original petitions, and cover about 25 percent of U.S. steel imports. DOC, following the applicable legal provisions and standard agency practice, has proceeded with the normal processing of the cases (including questionnaires, detailed explanations of procedures, and a system for handling specific problems of individual company-respondents). So far, all the foreign governments involved (including the European Communities Commission) appear to be cooperating fully.

In February, domestic steel producers filed additional antidumping or countervaililng duty complaints against wire rod producers in Argentina, Belgium, Brazil, France, South Africa and Venezuela. Additional cases alleging unfair subsidization of stainless steel bar and rod from Spain and wire nails from Korea, and dumping of stainless steel pipe and tube from Japan, were also filed this year. In addition, on February 26, USTR accepted a Section 301 petition from the specialty steel industry alleging that five countries (France, Italy, Sweden, Austria and the United Kingdom) have unfairly subsidized their specialty steel producers. USTR will now begin bilateral consultations with these foreign governments on the alleged subsidy practices, and within eight months make a recommendation to the President.

The next USG action in the major steel cases (those filed January 11) is the DOC preliminary determination of dumping or subsidization. The subsidy preliminary is due April 6 but can, and probably will, be extended to June 11. The dumping preliminary is due June 21, and can be extended to August 9. At the time of the DOC preliminary, importers must post bond for the amount of the estimated dumping or countervailing duties, which has a substantial "chilling" effect on trade in those products affected.

U.S. Steel Imports and State of Domestic Steel Industry

Steel imports in 1981 totalled 19.9 million tons (19.2 percent of the U.S. market), up from 15.5 million tons (16.3 percent products share) in 1980 and 17.5 million tons (15.3 percent market share) in 1979. Imports peaked in August at a record 2.2 million tons and have not substantially declined. December's 1.6 million tons seemed to indicate that imports were falling in lagged response to the decline in U.S. steel demand; the 2.0 million tons imported in January, despite the closing of the Great Lakes, brings this assessment into question.

Continuing high imports come at a time of weakness in the U.S. market. Domestic capability utilization stood at 59.3 percent during January, up slightly from 58.6 percent in December. Utilization rates have not varied significantly during February. During the week ending February 13, approximately 67 thousand steel workers (about 15 percent of the steel work force) were on furlough, little changed over the previous five weeks.

There is some concern that foreign suppliers will rush to bring steel into the United States to beat the imposition of antidumping or countervailing duties. DOC is closely monitoring steel imports for any signs of such behavior, and has warned importers that they may be liable under our statutes for retroactive duties if such behavior is observed.

DOC Response: Carry Investigations to Conclusion

We have repeatedly stated our intention to carry the antidumping and countervailing duty investigations through to conclusion. We have, nonetheless, informed foreign officials that we are willing to listen to any proposals which fit within the statutory provisions for settlement of cases short of final determination. High officials of the European Communities have indicated that they intend to cooperate in the investigations, and have stated that they believe they can prove that their producers have not violated our trade laws. While this remains to be seen (from information currently in hand it seems certain that significant subsidies will be found in several countries; the "wild card" is the ITC final injury determination), we welcome and encourage this attitude.